api INSTRUMENTS COMPANY

Annual Report 1967

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ANNUAL REPORT 1967

The Record in Brief

	1967	1966
Net sales	$9,169,990	$8,442,131
Federal income taxes	302,700	432,200
Net earnings	372,321	495,753
Earnings per share	.73	.99


David T. Morgenthaler


John D. Saint-Amour


Robert H. Pugsley


Harry W. Mergler


George J. Crowdes, Jr.


Thomas H. Conner


Ernest O. Myers


Myron W. Ulrich


John P. Isham

BOARD OF DIRECTORS

David T. Morgenthaler, Chairman
John D. Saint-Amour
Robert H. Pugsley
Harry W. Mergler

OFFICERS

John D. Saint-Amour
President

Robert H. Pugsley
Vice-President—Marketing

George J. Crowdes, Jr.
Vice President—Engineering

Thomas H. Conner
Vice President—Finance
Treasurer

Ernest O. Myers
Vice President—Manufacturing

Myron W. Ulrich
Secretary

John P. Isham
Controller

TO OUR STOCKHOLDERS, EMPLOYEES AND FRIENDS:

Although the latter half of 1967 showed great improvement over the unsettled early months, profits for the year were disappointing.

Spending for long-range programs was one factor adversely affecting net earnings. Another was a somewhat slower rate of growth than expected. Also, larger-than-normal write-off of inventory was required at year end. Inventory of certain items was excessive because better components have become available.

Shipments were up, reaching the highest level ever at $9,169,990. This represented a gain of 9 per cent over the previous high of $8,442,131 in 1966.

Net income of $372,321, or 73 cents per share, was down 25 per cent from the high of $495,753, or 99 cents per share, in 1966. Earnings per share in 1967 were diluted slightly because conversion of debentures increased the number of outstanding common shares by approximately 18,000.

The quarterly dividend of 10 cents per share was paid during 1967, with the total payout of 40 cents equal to that in 1966.

The difficult period early in the year was directly caused by high overhead costs. In anticipation of the need to keep up with the strong sales tone that prevailed during much of 1966, we increased our work force and expanded certain supporting facilities.

However, general industry-wide softness developed in late 1966 and our expansion proved excessive. Adjustments were made as quickly as possible and overhead was reduced to a budgetary level commensurate with needs.

GROWTH IN SOPHISTICATION

With our long-range plan calling for controls to exceed 50 per cent of total sales by 1969, 1968 will witness continuing emphasis on new and better controls of various kinds. Besides being more profitable, these instruments clearly are the shape of things to come in our business.

API's increasing skills in solid-state electronics, including the use of integrated circuits, are becoming more apparent. Until this year, we tended to add electronics to instruments that were basically electromechanical. In view of our fine reputation for precision and reliability in meters and meter-relays, we will probably never abandon our efforts in these fields. In the area of controllers, however, we are directing more of our capabilities toward all-solid-state designs.

In the electronic industry, "digital readout" has passed the fad stage and has become almost a necessity in panel instruments. It simply means that an instrument displays the value of a signal at a given moment in digits instead of a pointer

position on a scale. The convenience and utility of such a display is obvious. It is also far more accurate, especially in view of the tricks often played by the human eye.

Late in 1967, we concluded arrangements to introduce a digital panel meter early in 1968—shortly before this report was distributed. This new instrument has a number of important technical advantages, including exceptional stability and possibly the smallest panel space for instruments of its type. We believe its combination of features and price makes it superior to any competitive instrument.

To market this new meter, and to develop other digital indicating and controlling devices, a Digital Products Division has been formed. In view of the rapidly growing demand for digital instruments, this new division is bound to become increasingly important in the future.

CONTROLLERS FOR PROCESSING

Another line of instruments with great potential is our 225 series of temperature controllers, intended primarily for processing industries. These all-solid-state controllers, which control by actuating highly advanced devices, such as silicon-controlled rectifiers (SCR's), maintain temperatures within ½-degree F. of the desired level. Performance of this type can hardly be surpassed.

Our popular line of economical Compack controllers, which gained outstanding acceptance in a short time, has been expanded through the addition of models for controlling speed and pressure. Special sensors and circuitry are required for measuring and controlling these variables and until now our standard instruments have not been suitable for this purpose without extensive modification.

While developments in our standard panel meters and meter-relays are not likely to be as spectacular as those in electronic instruments, there is still a large continuing market for such devices. Our reputation as the "quality line" should insure a base in these markets for an indefinite time to come.

GEOGRAPHICAL EXPANSION

Sales offices in Chesterland, up-state New York and Canada were expanded and strengthened in anticipation of greater results from those areas.

Although our new Canadian plant reported a small loss in 1967, because of start-up costs, training and similar problems, it has now begun to operate in the black. Demand for our products is strong in Canada and the number of standard products manufactured there is being steadily expanded.

OUR PRIME ASSET—PEOPLE

An executive with impressive experience and an exceptional record of achievement, David T. Morgenthaler, has been elected Chairman of API's Board of Directors. Mr. Morgenthaler, a director of API since 1964, was president of Foseco, Inc., for 10 years.

Mr. Morgenthaler will be available for consultation on specific management problems, especially long-range planning for growth.

Earlier in the year, Dr. Harry W. Mergler, director of the Digital Systems Engineering Laboratory at Case Western Reserve University, was elected a director. He succeeded William T. Robbins, a director since 1957.

Dr. Mergler, who is also a consulting member of our Executive Product Planning Committee, has already contributed valuable ideas. Among other things, he has been active in API's entry into the digital instruments field.

Ernest O. Myers was elected to the new position of Vice President-Manufacturing. Mr. Myers was most recently Manufacturing Manager and he has shown a talent for organizing our many production efforts.

Other key management positions filled this past year included those of Manufacturing Manager for the new controls plant and Chief Manufacturing Engineer.

Efforts throughout the year to increase productivity, through better industrial engineering, have paid off, with efficiencies of individual units improving beyond our expectations. It is especially heartening that the employees whose work is being studied, and frequently redirected, are accepting the program with enthusiasm.

During 1968 improved methods and standards will continue to go into effect until the whole company has been reviewed toward the end of the year. We expect highly beneficial results as this program continues.

THE YEAR AHEAD

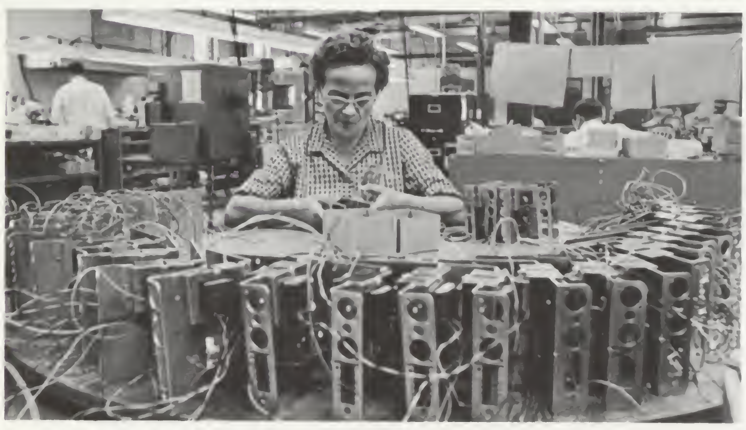
In view of the cloudiness of many economic predictions for 1968, any statement about the near future must be cautious.

We believe, nevertheless, that our increasingly technically-oriented position in the lively instrument market should keep us pointed upward. In 1968, we plan for increased sales and we will concentrate our efforts toward higher earnings.

Sincerely,

John B Saint-Amour

John D. Saint-Amour,
President



People and Products—A digital panel meter and a solid-state temperature controller are two of API's newest products (top left). Patience and precision are the watchwords with meter movements (top right). Constant testing and evaluation maintain quality (center). Controller chassis are being assembled in bottom view.

API TODAY

API Instruments designs and manufactures indicating and controlling instruments, both electrical and electronic. These instruments are used to measure all common phenomena that can be translated into an electrical signal. Practically every sizable manufacturer, military installation and research establishment in the country is among API's 5,000 customers.

Over the past two decades API has contributed importantly to the instrumentation connected with each succeeding trend of technology. API's instruments have been conspicuous in the military warning systems built after World War II; in nuclear installations; in the spread of automation throughout industry; in the growth of synthetics and other products of automatic processing, and finally, in the rapid growth of computerization and other aspects of electronic data processing.

During the years when panel meters and meter-relays were API's main concern, the company became known as the most innovative in its segment of the instrument industry. With emphasis now swinging toward self-contained controllers and solid-state electronics, API is pushing research and engineering in the same tradition.

Three relatively new lines of instruments, all radically different from API's earlier directions, seem likely to experience the greatest growth in the immediate future. These include temperature controllers with all-solid-state design; very small digital readout panel meters, and infrared thermometers for non-contact sensing and control of temperatures over considerable distances.

A GROWTH COMPANY

API's growth has been steady over the years, and it is now a large operation by many standards. More than 700 employees work in two plants with total floor space of close to 100,000 square feet. Another 100,000 square feet is planned for the new controls division plant, built two years ago.

Both plants are located in Chesterland, Ohio—with all the big-city advantages close by (Cleveland), but with ideal residential and rural living opportunities short minutes from the plant.

Along with this growth, API has retained an atmosphere that makes it a pleasant place to work. Each week, a different group of employees meets with the president to discuss company policies that concern them, and to pass along their suggestions for changes. The objective is to prevent any dissatisfaction from developing into real problems. Because of this give and take tradition, employee relations are among the most harmonious to be found.

API stock was offered to the general public in September, 1957. Its shares are traded on the American Stock Exchange. The company now has more than 3,500 stockholders, located in practically every state and many foreign countries.

api INSTRUMENTS COMPANY AND SUBSIDIARY

TEN-YEAR FINANCIAL SUMMARY

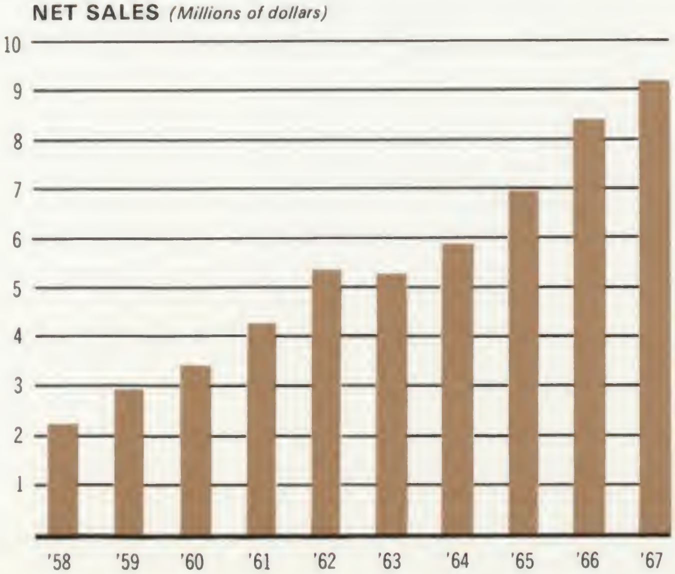
	1967	1966	1965	1964	1963	1962
Net Sales	$9,169,990	$8,442,131	$6,942,031	$5,812,783	$5,346,356	$5,371,164
Earnings before Federal taxes on income	675,021	927,953	843,198	692,244	411,896	684,442
Provision for Federal taxes on income	302,700	432,200	404,000	340,000	208,000	351,500
Net earnings	372,321	495,753	439,198	352,244	203,896	332,942
Earnings per share (A)	.73	.99	.88	.71	.41	.67
Pro forma earnings per share (B)	.70	.92	.82	.67	.42	.60
Cash dividends per share	.40	.40	.35	.30	.05	.10
Additions to property, plant and equipment	107,773	532,737	529,894	120,631	165,007	129,276
Provision for depreciation	194,337	175,309	152,232	138,713	135,946	128,516
Current assets	3,485,411	3,259,316	3,045,808	2,994,188	2,856,240	2,943,954
Current liabilities	955,390	1,016,952	782,314	654,515	537,306	664,389
Working capital	2,530,021	2,242,364	2,263,494	2,339,673	2,318,934	2,279,565
Long-term debt payable	787,000	1,029,000	1,054,000	1,075,000	1,273,570	1,250,000
Book value per share (C)	6.17	5.58	4.95	4.41	4.00	3.89
Stockholders' equity	3,225,005	2,797,294	2,470,904	2,197,571	1,994,725	1,961,834

Notes: (A) Stated on the basis of average shares outstanding with the public at the beginning and end of the respective periods, adjusted for stock split (200% in 1959) and stock dividends (5% in 1960 and 4% in 1963).

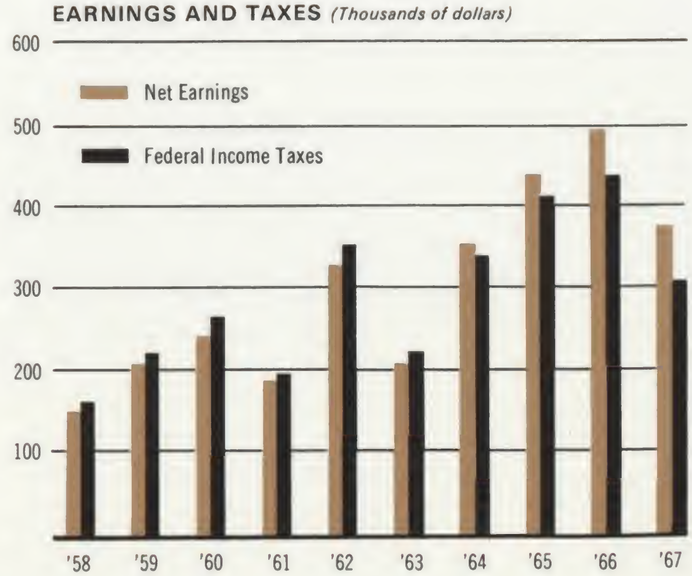
(B) Assuming conversion of all outstanding debentures issued in 1962.

(C) At close of the respective years adjusted for the stock split and stock dividends.

NET SALES *(Millions of dollars)*

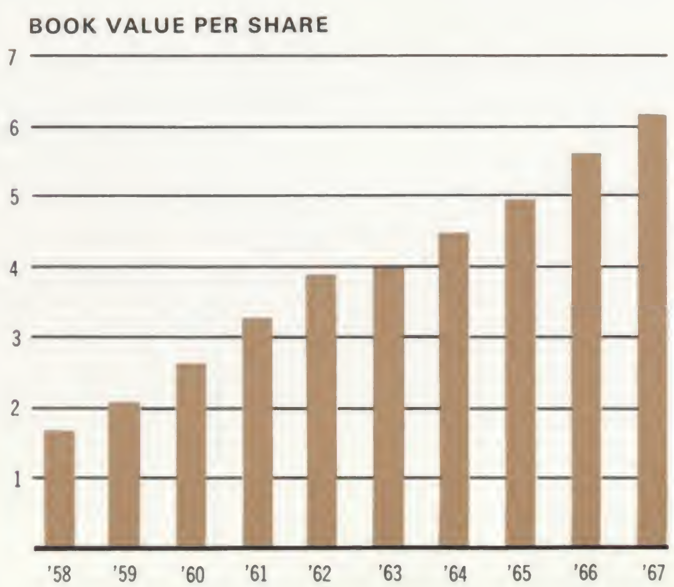


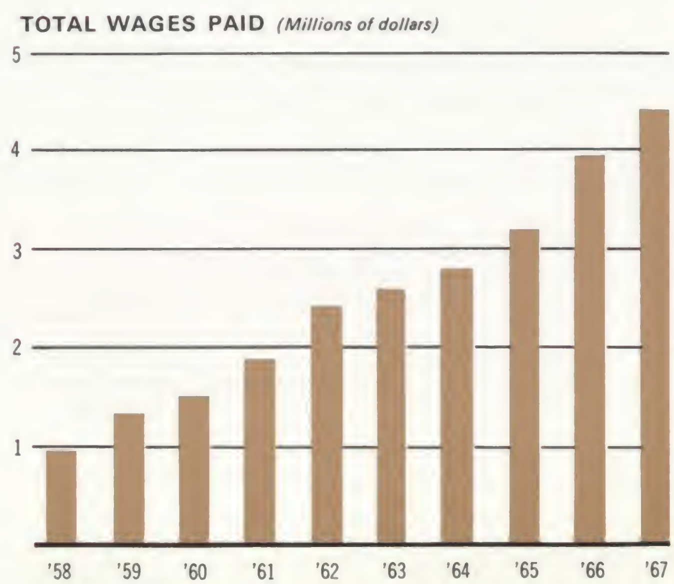
EARNINGS AND TAXES *(Thousands of dollars)*



1961	1960	1959	1958
$4,161,389	$3,400,579	$2,914,170	$2,157,540
378,889	502,285	416,830	308,119
190,000	260,227	214,977	156,969
188,889	242,058	201,853	151,150
.39	.51	.44	.33
	.10		.06
480,732	71,880	209,363	41,347
99,802	64,568	48,185	43,518
1,682,887	1,323,270	980,811	782,434
541,693	391,616	376,326	323,635
1,141,194	931,654	604,485	458,799
305,000	100,000	150,000	53,269
3.32	2.75	2.11	1.69
1,647,500	1,327,858	962,833	760,981

Medical electronics is a big market for API instruments, as illustrated by their use in this artificial kidney system. The machine enables a patient to perform his own dialysis (removal of toxins from the blood stream). API controllers maintain temperature of solutions within close limits. They also trigger alarms and shut down the pump if the machine malfunctions.





api INSTRUMENTS COMPANY AND SUBSIDIARY

CONSOLIDATED BALANCE SHEET

ASSETS	December 31, 1967	1966
CURRENT ASSETS:		
Cash	$ 212,540	$ 138,657
Accounts receivable, less allowance for doubtful accounts of $14,800 in 1967 and $13,540 in 1966	1,403,449	1,360,447
Inventories, at the lower of cost (first-in, first-out) or market	1,828,796	1,734,867
Prepaid expenses	40,626	25,345
TOTAL CURRENT ASSETS	$3,485,411	$3,259,316
OTHER ASSETS:		
Non-current receivable	$ 27,952	$ 34,952
Cash surrender value of life insurance—net of loans	8,117	842
Unamortized debenture expense	26,642	42,298
	$ 62,711	$ 78,092
PROPERTY, PLANT AND EQUIPMENT—at cost:		
Land	$ 98,741	$ 98,741
Buildings and improvements	1,450,684	1,440,812
Machinery and equipment	630,489	612,593
	$2,179,914	$2,152,146
Less accumulated depreciation	760,641	646,308
	$1,419,273	$1,505,838
	$4,967,395	$4,843,246

See notes to financial statements.

NOTES TO FINANCIAL STATEMENTS *Year ended December 31, 1967*

A—PRINCIPLES OF CONSOLIDATION

The accompanying consolidated financial statements include the accounts of the company and its wholly-owned subsidiary, API Instruments Canada, Limited, after eliminating intercompany accounts and transactions. All accounts have been translated at the average rate of exchange for the year.

B—5¼% CONVERTIBLE SUBORDINATED DEBENTURES

The convertible subordinated debentures are due September 1, 1972. They are convertible into common shares at $13.46 per share (with antidilution adjustment provisions) and through August 31, 1967 were redeemable at the company's option wholly or in part at a premium of 5%. Thereafter, the premium decreases at a rate of 1% per annum. Bonds in the amount of $242,000 were converted into common stock during 1967. At December 31, 1967 there were reserved for conversion of the debentures 58,470 shares of the company's authorized but unissued common stock.

C—STOCK OPTIONS

Under the company's stock option plans, options are granted at not less than fair market value at date of grant. The options are for a period of five years and are exercisable 18 months after date of grant except that not more than 40% may be exercised within two years from date of grant, and 20% each year thereafter during the remaining option period. Cumulative provisions apply with respect to any period in which that portion of the option was not exercised.

During the year ended December 31, 1967, 2,513 shares of common stock were issued for $18,201 under the company's stock option plans. Changes in stock options during the year were as follows:

LIABILITIES AND STOCKHOLDERS' EQUITY	December 31, 1967	1966
CURRENT LIABILITIES:		
Note payable to bank	$ 200,000	$ 150,000
Accounts payable	312,645	306,961
Payroll and other taxes	125,763	131,444
Salaries, wages and commissions	173,151	189,021
Interest	15,062	20,797
Other	11,103	10,666
Federal taxes on income	117,666	208,063
TOTAL CURRENT LIABILITIES	$ 955,390	$1,016,952
5¾% CONVERTIBLE SUBORDINATED DEBENTURES (Note B)	$ 787,000	$1,029,000
STOCKHOLDERS' EQUITY:		
Common stock, par value $1 per share: Authorized 750,000 shares (Notes B and C) Issued 529,644 shares in 1967 and 509,173 shares in 1966 (including 6,934 shares held in treasury)	$ 529,644	$ 509,173
Additional paid-in capital	1,082,688	842,958
Retained earnings	1,651,680	1,484,170
	$3,264,012	$2,836,301
Less 6,934 shares of common stock held in treasury, at cost	39,007	39,007
	$3,225,005	$2,797,294
	$4,967,395	$4,843,246

	Shares	
Options outstanding at January 1, 1967		12,288
Less:		
Options exercised at prices from $5.26 to $10.88 a share	2,513	
Options terminated	1,780	4,293
Options outstanding at December 31, 1967, at prices ranging from $7.38 to $14.50 a share (3,577 shares exercisable)		7,995
Shares available for future grants		19,530

D—PENSION PLAN

The company's contributory retirement pension trust covers all employees who have at least three years of service and who desire to make the required contribution toward the acquisition of life insurance contracts providing retirement benefits. The company pays an amount equal to twice the amount contributed by the employee. Total pension expense was $56,576 in 1967 and $51,614 in 1966. No past service liability exists under the plan.

api INSTRUMENTS COMPANY AND SUBSIDIARY

CONSOLIDATED STATEMENT OF EARNINGS

	Year Ended December 31, 1967	1966
NET SALES	$9,169,990	$8,442,131
COSTS AND EXPENSES:		
Cost of products sold, exclusive of depreciation, amortization and taxes	$6,421,801	$5,681,391
Selling, administrative and general expenses	1,471,861	1,312,185
Depreciation	194,337	175,309
Taxes, other than federal taxes on income	283,925	257,922
Provision for uncollectible receivables	38,375	28,797
Interest expense (including amortization of debenture expense)	84,670	69,870
	$8,494,969	$7,525,474
Interest income		11,296
	$8,494,969	$7,514,178
EARNINGS BEFORE FEDERAL TAXES ON INCOME	$ 675,021	$ 927,953
PROVISION FOR FEDERAL TAXES ON INCOME	302,700	432,200
NET EARNINGS	$ 372,321	$ 495,753
Net earnings per share of common stock (based on average shares outstanding, 512,474 shares in 1967 and 500,933 shares in 1966)	$.73	$.99
Pro forma net earnings per share of common stock assuming conversion of all outstanding debentures (579,924 shares in 1967 and 578,291 shares in 1966)	$.70	$.92

See notes to financial statements.

CONSOLIDATED STATEMENT OF RETAINED EARNINGS

	1967	1966
BALANCE, beginning of the year	$1,484,170	$1,188,646
Net earnings for the year	372,321	495,753
	$1,856,491	$1,684,399
Cash dividends—$.40 a share in 1967 and 1966	204,811	200,229
BALANCE, end of the year	$1,651,680	$1,484,170

See notes to financial statements.

CONSOLIDATED STATEMENT OF ADDITIONAL PAID-IN CAPITAL

	1967	1966
BALANCE, beginning of the year	$ 842,958	$ 814,704
Excess of proceeds received over par value of common shares (2,513 shares in 1967 and 757 shares in 1966) sold upon the exercise of stock options (Note C)	15,688	5,110
Excess of face value of 5¾% convertible subordinated debentures over par value of common shares issued upon conversion (17,958 shares in 1967 and 1,855 shares in 1966) (Note B)	224,042	23,144
BALANCE, end of the year	$1,082,688	$ 842,958

See notes to financial statements.

CONSOLIDATED STATEMENT OF SOURCE AND APPLICATION OF FUNDS

	Year ended December 31, 1967	1966
FUNDS PROVIDED:		
Operations:		
Net earnings for the year	$ 372,321	$ 495,753
Charges to net earnings requiring no expenditure of funds:		
Depreciation	194,337	175,309
Amortization of debenture expense	15,657	8,669
Write down in non-current receivable	7,000	
FROM OPERATIONS	$ 589,315	$ 679,731
Proceeds from stock options exercised	18,201	5,867
Proceeds from loans on life insurance policies		36,540
	$ 607,516	$ 722,138
FUNDS APPLIED:		
Cash dividends paid	$ 204,811	$ 200,229
Net additions to property, plant and equipment	107,773	532,737
Increase in cash surrender value of life insurance	7,275	10,302
	$ 319,859	$ 743,268
INCREASE (DECREASE) IN WORKING CAPITAL	$ 287,657	$ (21,130)
SUMMARY OF WORKING CAPITAL:		
Current assets at end of the year	$3,485,411	$3,259,316
Less current liabilities at end of the year	955,390	1,016,952
WORKING CAPITAL AT END OF THE YEAR	$2,530,021	$2,242,364
Working capital at beginning of the year	2,242,364	2,263,494
INCREASE (DECREASE) IN WORKING CAPITAL	$ 287,657	$ (21,130)

See notes to financial statements.

ACCOUNTANTS' REPORT

The Stockholders and Board of Directors,
API Instruments Company, Chesterland, Ohio

We have examined the accompanying consolidated balance sheet of API Instruments Company and subsidiary as of December 31, 1967, and the related statements of earnings, retained earnings, additional paid-in capital, and source and application of funds for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the consolidated financial position of API Instruments Company and subsidiary at December 31, 1967, and the consolidated results of their operations, and the source and application of funds for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Touche, Ross, Bailey & Smart

Cleveland, Ohio
March 1, 1968

Certified Public Accountants.

api INSTRUMENTS COMPANY

CHESTERLAND, OHIO 44026